The Impact of Ownership on the Grameen Bikas Banks' Current and Future Performance

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Introduction

Under funding by USAID/Nepal through the IRIS project, a team of consultants was hired from December 1996 to February 1997 to assess the performance of the majority government-owned Grameen Bikas Banks (GBBs) in Nepal, and to determine whether a change in their ownership might make them more effective. The consultancy team consisted of two members: Dr. Muzammel Huq, General Manager of the Grameen Bank in Bangladesh, and Mr. Peter Boone, economist and financial analyst from SRI International in the United States.

Study Objective

The consultants were asked to review the performance of the five majority government-owned GBBs. They were also requested to compare the GBB performance with the Grameen replications controlled by Non-Governmental Organizations (NGO Grameens.) The scope of work included an assessment of whether an ownership change would have a favorable impact upon the GBBs' mission to provide economic opportunities to poor women, through the delivery of small-scale loans. Should such a change be considered appropriate, the consultants were asked to assess various methods of ownership transfer, and to suggest those most feasible under the current circumstances.

Grameen Bikas Bank Development and Approach

In Nepal: the Grameen rural finance model was established in 1993, following the model of the original Grameen Bank in Bangladesh. The Bangladesh model successfully demonstrated over a twenty-year period that poor women can be identified: reached, organized and served in a sustainable way. The Grameen Bank operations are based on a low--cost, high-volume delivery of small loans, guaranteed by solidarity groups rather than collateral. Under these conditions, the pool- can bc trustcd to pay back fully, and almost always on timc. In Bangladcsh, womcn's access to credit increased their incomes substantially, improved their living conditions, and gave the borrowers higher status and dignity in their families and communities.

The Grameen model has been replicated in Nepal via the establishment and operation of five majority government-owned Grameen banks (GBBs) and two NGO Grameens: Nirdhan and the Centre for Self-Help Development (CSD). The rationale for the establishment of these banks was to offer a proven model of low cost, sustainable, credit-delivery system to poor women who were not being reached by other programs. The Nepal Rastra Bank (the central bank of Nepal) established the government replications, and is majority shareholder in the five government-owned GBBs.

The basic features and principles of the GBB and NGO Grameen replications in Nepal are as follow-s:

- They have a *well-defined target group*. Any poor rural women: as defined by women from households of less than 0.6 hectares of land in the Terai (low lands) region. or less than 0.5 hectares of land in the hills, is eligible to join a group.'

- They adopt *an area upproach* whereby the staffs concentrate their lending and outreach activities in a Village Development Committee (VDC) area. The VDC is the smallest unit of local government.

- They use a highly *organized delivery system*, as the banking activities take place in the communities where the women members live. All banking transactions take place openly and publicly at the weekly center meetings. A center is a federation of a maximum of eight groups (i.e., maximum of 40 women). A branch office administers about 50 centers, and an area office supervises about five branch offices.

- They follow a *group lending approach* in which a group of five poor women organize themselves in a group, and elect a chairperson among themselves.

- The Grameen replications follow a *2+2+1 system* whereby initially only two members receive loans. After eight weeks two members receive loans, provided the first two are able to pay back their weekly installments regularly. Finally, the chairwoman receives a loan after sixteen weeks from the date of the first loan disbursement.

- The *size of the loans is small.* The first loan is a maximum of Rs. 5,000 (US$ 89) After full payment of the first loan after a one-year period of weekly payments. members can receive a second loan of up to Rs. 10,000 (US$ 179).

- *The Grameen replications don't require physical collateral.* Loans are extended to individual group members under a group guarantee system that uses peer pressure,

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[1] IRIS and its consultants observed in the field that the GBBs have a higher slippage rate in meeting target lending criteria than the NGO Grameens. IRIS estimates a 20 percent slippage rate for the Eastern Grameen Bank and a 5 percent slippage rate for the Far Western Grameen Bank. IRIS calculates that CSD and Nirdhan have slippage rates below 5 percent in meeting their target lending criteria. In addition, the NGO Grameens tend to have tighter criteria for membership, such as the requirement that no member be married to anyone with permanent wage employment.

persuasion, ad support from the group to ensure loan repayment. Group savings are sometimes tapped to ensure the high repayment rate.

- They follow a *weekly repayment* system, through which interest and principal payments are due on a w-eekly basis for 55 weeks.

- The Grameen replications are *flexible about economic activities undertaken with loan proceeds.* Borrowers, in consultation with their groups, are free to decide what type of economic activities they wish to undertake. To date, most of the loans disbursed have been used for small trading, livestock, and other small farming activities.

GBB and NGO Grameen Performance to Date

As of mid-December 1996,[2] the five government-owned GBBs and the two NGO Grameens had reached a total of 54,936 poor women borrowers through a network of 11 area offices: 95 unit offices, and 2,089 centers. A total of 11,545 groups with 57,355 women members were formed in 377 village development committees (VDCs) spread over 22 of Nepal's 75 districts: largely in the Terai zone.

Cumulative loan disbursements for these seven banks amount to Rs. 689 million (US$ 12.3 million), of which the government-owned GBBs accounted for 90 percent as of end-1996. The largest GBB, the Eastern Grameen Bank, accounts for 63 percent of the total cumulative disbursements of the GBBs and NGO Grameens to date. The average size of loans disbursed by the seven banks is Rs. 13,920 (US$ 249), indicating that some borrowers have taken second and third loans.

As of mid-December 1996, none of the GBBs nor the NGO Grameens showed any overdue repayments. This record of repayment is very surprising to many outside observers who are more familiar with rural credit programs with much lower recovery rates. The record is similar to that of the Grameen Bank of Bangladesh, and is largely due to strict adherence to the concepts of group solidarity and group guarantees of the loans. In the orientation/training program provided to borrowers as part of the process of organizing into self-selected groups, the absolute importance of full and on-time repayment to the financial viability of the program is emphasized. Livestock insurance and use of the group fund to deal with payment problems also explains the solid repayment record.

Group savings are compulsory under the Nepali GBB and NGO Grameen system, while personal savings are voluntary. Each borrower is supposed to contribute 5 percent of the loan

[2] All Grameen replications in Nepal follow the Nepali calendar, which has different month-ends than the American calendar. Data provided was the latest available from the organizations at the time of reporting.

amount to group savings, and is also expected to contribute to her personal savings account on a weekly basis. As of mid-December 1996, savings in the group funds of the four[3] government and two NGO Grameen replications stood at Rs. 40.8 million (US$ 7 19,000.) Half of the group fund can be used to meet temporary emergencies or needs of borrowers. In most cases, these group fund loans are interest-free. The group sayings level is highest at the Eastern Grameen Hank with 63 percent of the total GBB and NGO group savings coming from that Bank.[4] Personal savings in the GBBs and the NGO Grameens was Rs. 4.3 million (US$ 75.77 1) as of mid-December 1996.

Targeting Poor Women and Impact on Women's Empowerment

Nepal is one of the poorest countries in the world, with a GNP per capita of US$ 200.[5] The percentage of the population living under an international definition of poverty is about 42 percent, and about 15 percent at the lower end of this group would be considered to be "hard-core poor." Some eighty percent of the population of Nepal lives in rural areas. Evidence from income, consumption, and nutritional surveys suggests that women and children are the most severely affected by poverty in Nepal.

All of the borrowers met by the consultant team met the selection criteria described on page 2, and the program is clearly serving the needs of poor rural women. However, the team observed that these lending criteria do not necessarily target the hard-core poor -- for instance the landless poor -- as the highest-priority target group. While some of the hard-core poor are being reached by the program, it does not give them special importance. At this time, the hard-core poor arc only being served in small nutnbers by the GBBs and NGO Grameens.

One of the reasons for this observation is the principle that the credit system must be financially viable. In order to meet financial viability goals, large numbers of borrowers must be reached reasonably rapidly in relatively concentrated areas (horizontal expansion and efficiency.) Those at the very bottom of the income scale are often reluctant **to** borrow, and **intensive efforts** are necessary in order to reach and involve them. In addition, they tend to borrow much smaller amounts, thus increasing the relative transactions costs and requiring a larger client base to cover costs.

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[3] The fifth Government owned GBB (Central Region) was started in January 1997.

[4] The Eastern Grameen Bank's group savings represent the same proportion of total GBB and NGO Grameen savings (63%) as its share of total disbursements (63%). This is expected since group savings are compulsory and are set at five percent of the loan disbursement amount.

[5] World Development Report, the World Banh. 1996

One hundred percent of the loans disbursed by the GBBs and the NGO Grameens have been made to fifty-live thousand women over the last three years. In addition to empowering women as clients. the Cirameen replications in Nepal are also empowering them as professionals, Women represent 30 percent of the staff of the GBBs and the NGO Grameens. compared with a much smaller number of women staff at the Grameen Bank in Bangladesh (about 10 percent.)

No major socio-economic impact studies have been undertaken on the Nepali Grameen Hank lending programs to date. Observations by Professor Latifee of the Grameen Trust.[6] and confirmed by the current consultancy team. are that in three years of operation the impact on the life of borrowers is positive. The women borrowers have substantially increased their incomes. and many of them are able to save through the group savings and personal savings programs. The training program for borrowers focuses on savings. cooperation. and use of loans for the betterment of their lives. The women have learned to sign and have stated that the program has provided them with more confidence in their abilities to contribute and to earn and control money. as well as having increased decision-making power in the households.

Some of the group activities under the Grameen lending programs have been tied to other self-help programs. such as a UNICEF project that focuses on literacy training. seed and sapling distribution. tubewell loans. and other social development programs. These activities are considered to be significant in the empowerment of poor women in Nepal. However. the Grameen replicants generally support a "micro-finance services only" approach. recognizing that in other countries as well as in Nepal. combining social and financial services has been problematic.

The experience of Bangladesh and anecdotal experience from Nepal indicates that a certain number of the GBB and NGO Grameen loan funds made to women were actually passed on to their husbands. and/or the women made joint decisions about the funds with their spouses. and share the work with them. It is not known how extensive this practice is in Nepal. When the husbands use the funds. the women have the Full responsibilities for repayment with little or no control over the economic activity. This practice can be minimized in future through more intensive bank training on use of the funds during borrower orientation. through group coordination. support. supervision techniques. and through gender work within the organizations -- such as the gender trainings currently being provided by IRIS under USAID funding.

Financial Sustainability of the **GBBs**

Financial sustainability or self-sufficiency- is defined as the ability of a financial institution to cover all its administrative and financial costs without the benefits of grants. subsidies. concessional borrowings. or special preferential legal conditions. For the Grameen replications. this translates into the ability to cover operating costs (service delivery cost. plus loan loss) and

[6] See the "Evaluation Report on Grameen Bikas Banks in Nepal" by H.I. Latifee. 1994.

capital costs (interest cost) from their loan interest income. A GBB or an NGO Grameen is said to have reached sustainability when its interest income exceeds its operating and capital costs. Based on the experience of the Grameen Bank in Bangladesh, this is an objective that may take from three to five years for a branch to reach, and seven to 10 years for an organization to achieve. Once financial sustainability is reached, it is still a continuous challenge to maintain it.

Please note: the difference between financial sustainability and financial viability is crucial. Sustainability is the achievement of a level of loan interest income that covers all costs; viability means that the organization can also cover losses incurred during the period before it reaches financial sustainability, and maintain full self-sufficiency over time. Thus the data below must be viewed with caution. References to levels of self-sufficiency do not take account of previous losses accrued by the organizations, nor how they have dealt with these (eg by donor financing or debt.)

Table 1 in Appendix A shows that the GBBs have zero bad debt cost to date. The performance of the NGO Grameens has been similar: those organizations also enjoying 100 percent repayment records to date (see Table 2, Appendix A.) Together, the GBBs and the NGO Grameens have enjoyed a low cost of capital to date, with borrowings from commercial banks typically ranging from 6 to 8 percent (see Table 3, Appendix A.) However, by late 1996, the GBB and NGO Grameen borrowing costs were rapidly climbing to 11 percent, or close to the NRB Treasury bill rate.[7]

Information on service deliver-y costs (see Table 4, Appendix A) indicates that, over the last three years, the efficiency and financial sustainability of the banks has been improving significantly, as each bank has reduced its year-on-year delivery costs. For example, the Eastern GBB (EGBB), one of the most cost-effective of all Grameen replications in Nepal, has reduced its service delivery cost from 20 paisa[8] per rupee disbursed in 1993/94 to 10 paisa for every loan disbursed in 1995196. With no loan losses, a service-delivery cost of 10 percentage points, and a cost of capital of about 8 percent in 1995/96, the total operating and financial cost for EGBB was about 18 percent, versus a lending rate of 20 percent. This made the EGBB be slightly profitable by its third year of operation, with a financial self-sufficiency rate of 111 percent.[9] If these profits are maintained, the EGBB will recover losses incurred in the first three years of operations.

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[7] GBB and NGO Grameen costs of borrowing have been rising since mid-1996 because interest rates in general in Nepal. including treasury bills and commercial lending rates, have been rising during this time period. In addition to this general trend, the commercial banks may also be charging higher rates to cover their perceived risks of non-repayment by the GBBs and NGO Grameens. The commercial banks appear to be realizing that they can charge these rates and that GBBs and NGOs are accepting them.

[8] There are 100 paisa in a rupee.

[9] Defined as interest income/total costs (service delivery, plus loan loss, plus cost of capital)

Similarly, the NGO Grameen CSD reduced its service delivery cost from 43 paisa per rupee disbursed in 1993/94, to 11 paisa per rupee disbursed in 1995/96. With a cost of capital of some 8 percent in 1995/96, and a zero loan loss rate, CSD's total operating and financial costs were some 19 percent, versus income of20 percent. This gives CSD a financial sufficiency rate of some 105 percent in 1995/96. In the case of Nirdhan, service delivery costs have dropped from 49 paisa per rupee disbursed in 1992/3 to 16 paisa in 1995/6, and its total costs are about 24 percent versus income of about 20 percent, giving Nirdhan a financial self-sufficiency rate of about 83 percent for 1995/96.[10]

Despite this progress on sustainability, interest rates on loans have been rising in the short term. The EGBB, CSD, Nirdhan, and the other GBBs will need to either further reduce their service delivery cost and/or raise their lending interest rates to be financially viable in the future. A continued horizontal and vertical increase in loan volume will help lower unit delivery costs.

Other GBBs are further from reaching financial viability. For example, even though service delivery costs are steadily falling for the Far Western GBB, its service delivery costs (I 9 percent) plus loan loss (zero), plus fund cost (8 percent) mean that the bank only reached a financial self-sufficiency rate of 7 1 percent in 1995/96. The bank had accumulated losses of some Rs. 17 million (US$ 304,000) by mid-1996 (see Table 8, Appendix A.)

Capitalization of the GBBs

The government GBBs were initially capitalized at Rs. 30 million (US$ 535,000) per bank. In the first capitalization, 60 percent of the paid-up capital was provided by the Nepal Rastra Bank, 15 percent by His Majesty's Government, and the remaining 25 percent by commercial banks. (The commercial banks were allowed to apply this investment against their deprived sector lending targets as inducement to invest.) In a second capitalization? an additional Rs. 30 million of paid-up capital was injected into the GBBs, bringing the total paid-up capital to date of Rs. 60 million (US$ 1.07 million) per GBB (see Table 5 in Appendix A.)

Several of the GBBs have used their paid-up capital as a source of funds to meet their demands for loan funds, and to meet their operating costs. As a result of this development, several of the GBBs, particularly the Far Western Grameen Bank, have significantly eroded their capital base, resulting in a drop in their market value and net worth. If the Far Western Grameen share value were re-valued to reflect accumulated losses, the Bank's net worth would drop from Rs. 60 million (US$ 1.07 million) to Rs. 43 million (US$ 767,000).

[10] In February 1997, Nirdhan announced that it was increasing its interest rates to 25% per annum.

Impact of Ownership on the Management and Financial Performance of the Banks

Of the seven Grameen replications in Nepal, five are majority government-owned, and two (Nirdhan and CSD) are owned by NGOs. The private NGOs have been relatively free of government interference in the management and operations of the banks. The government-owned GBBs have not been free from political pressures, however.

The impact of government ownership on the management of the GBBs has manifested itself in several ways:

- The government GBBs have been willing to utilize an interest-rate subsidy for their borrowers, while the NGOs have decided not to accept the subsidy for concerns about sustainability and market distortion. The subsidy available to GBB borrowers amounts to 80 percent of the interest rate payable for loans under Rs. 5,000 (US$ 89), and 33 percent of the interest rate payable for loans up to Rs. 15,000 (US$ 267). The use of the subsidy by the government banks has made the NGO Grameens relatively less competitive when trying to attract borrowers. There is now a realization within the Government that this subsidy will become a growing burden on public finances, is not sustainable, and should be removed as soon as possible.

- If the subsidy is included in the analysis, the government-owned GBBs look much less financially viable than reported above. When the subsidy is included in the calculations, the banks' "true income" from interest payments (or income which is received directly from clients) drops substantially: for example, effective interest income on small loans less than Rs. 5000 (US$ 89) drops from 20 percent to 4 percent. The financial self-sufficiency ratios of these banks also drop from a range of 70-100 percent (without the subsidy impact) to about 15-25 percent with the subsidy impact. By including the real cost of the subsidy, the revenue generated by the banks drops sharply, while the cost of delivery remains the same as with the subsidy.

- The success of certain GBBs -- which has been associated with the large numbers of borrowers they have reached -- has led both of the main political parties to begin to see the banks as "vote banks." Both parties would like to claim the credit for the accomplishments to date of the GBBs, and mobilize members to support their parties. However, the consultant team feels that any further politicization of the banks could seriously jeopardize them, or even lead to their demise.

- The Board of Directors, including the Executive Director of each GBB and its Chairperson. are supposed to be elected for a term of four years. However, each of the three changes of government during the last three years has been followed by the replacement of the Executive Director and Chairperson of the GBBs, and often Board members as well.

- Several of the other top positions in the banks have been awarded to political party workers on the basis of their affiliation rather than their banking competence. This has led to serious instability of management, and has made it more difficult for the banks to focus on their mission -- reaching on a sustainable basis a maximum number of poor women borrowers.

- The decisions for locations of some branch offices and headquarters also appear to have been based on political -- rather than financial -- criteria. For example, the Far Western and the Mid Western GBBs operate in the same catchment area, and these banks will face difficulties attracting enough customers from the same region for both banks to be viable.

- In one of the GBBs -- the Eastern GBB -- the staff have organized themselves into two trade unions, each one affiliated with one of the two major political parties. The workers have expressed demands for higher benefits and allowances, more job security, specific postings, etc. While all workers have the rights to organize and to join unions, the attitude of the workers and their expectations about their employment conditions are far more consistent with the civil service than for a poverty alleviation organization. This could make it impossible for the GBBs to reach financial viability. In the Bangladesh Grameen Bank, workers' pay raises are directly linked to productivity increases, within the context of providing secure and sustainable credit to the poor.

- The staff/borrower ratio is considerably higher in the government-owned GBBs. Growth can slow when workers have (or demand) lower client/staff ratios. In addition, the salaries: particularly of the two largest government GBBs (Eastern and Far Western) are considerably higher than the NGO Grameens. The implications are clear: movement toward financial self-sufficiency will be slower, and the orientation will not be toward increases of borrower members under each staffer.

- At the Western and the Mid Western GBBs, proper recruitment procedures, including the placement of advertisements and conducting of examinations, were not followed for the hiring of several staff members. When a new Executive Director was appointed, he canceled these appointments on the grounds that proper procedures were not followed. The dismissed staff took their case to court. The court ruled in favor of the action to dismiss the employees. The net result of this situation on bank operations was negative: serious time was lost in the process, legal costs were incurred, retained staff were demoralized, and expansion programs were delayed. In addition, borrowers were concerned about changes in staffing: and an entirely new- set of staff had to be recruited and trained.

Regional Experience with Politicized Credit Programs

The experience of many countries in the region such as India, Bangladesh, Malaysia, and the Philippines has been that when government credit programs become politicized, it becomes impossible to maintain good credit discipline. There have been numerous cases in those countries and in Nepal (such as Nepal's SFDP, or the Masagana 99 in the Philippines) where government interference led to the following pattern:

- inefficient and costly operations;
- political patronage in the appointment of staff;
- the use of subsidies in place of good management and good credit discipline;
- government announcements of forgiveness of debt; and ultimately
- resulting poor repayment rates and unsustainability.

In several cases in South Asia, loans outstanding in large government lending programs have been completely written off, as politicians declared debt forgiveness or promised large subsidies to borrowers which in the end made repayment impossible. These approaches have always been short-sighted; in the absence of repayment there was no replenishment of capital, and therefore borrowers' access to new loans w-as severely restricted. Since good credit discipline is closely tied to borrowers' desire for continued lending, once good repayment is delinked from access to the next loan, the situation rapidly deteriorates into organizational failure.

The Need for Ownership Changes

The Nepal Rastra Bank (Central Bank), which has pioneered the concept and nurtured the GBBs to help tackle property reduction, needs a strong and professional owner/director body to stave off partisan interference and enable to the GBBs to expand and achieve sustainability. The Board of Directors and management must be capable of withstanding government pressure, which, if unchecked, could destroy the credit discipline and operational effectiveness built by the dedication of both the staff and the borrowers.

In order to increase the financial viability of the GBBs, improve efficiency and performance, and reach and empower more women, it is recommended that the government sell or transfer a majority of ownership of the GBBs to the private sector. The consultants suggest that the proposed ownership transfer take place within the next year. Time is of the essence. since another change of Board of Directors and Chief Executives is most likely to further polarize the GBBs along political lines. Government officials met by the consultants expressed their interest in moving quickly to a minority position, realizing that an immediate ownership change was vital to the future growth and development of the GBBs, and that these banks should not become "vote banks," or arenas where political tugs-of-war replace the genuine work of alleviating poverty.

The GBBs have so far done a remarkable job in reaching women with credit for self-employment. The Government's assessment -- which the consultants support -- is that with private ownership and management, the GBBs can reach about 200,000 women with credit and saving services by the year 2000. However, if government remains the majority owner the estimate of the number of borrowers reached will be much smaller -- in the range of 70,000 to 80,000 by the year 2000.

The ultimate owners of the GBBs should be the women borrowers. Other changes empowering women that are likely to accompany the ownership change in Nepal include the introduction of women borrowers to the Boards of Directors, an increase in the percentage of women staff from the current 30 percent, and an increase in the number of women in management positions in the GBBs.[11]

Given the initial levels of capitalization, (a total Rs. 300 million or US$ 5.35 million for the five government GBBs), and the current level of GBB borrower capital in group savings (about Rs. 41 million), it will clearly take a number of years before the borrowers will have saved up enough capital to buy a majority of shares in the banks, assuming the GBBs are valued at, or near, their current book value (Rs. 60 million or US$ 1.07 million) per GBB. The following section proposed options for the ownership transfer which address this concern.

Ownership Transfer Options

Five different options for ownership transfer are proposed by the consultants. Each of the options has its own strengths and weaknesses. We present below the major pros and cons of each of the ownership transfer options and summarize each of these in the table which follows this section.

It should be noted here that for each option, several share transfer mechanisms are possible. The first would be to sell the shares at book value. An alternative option would require that the shares be sold at a market adjusted value price, following a valuation by an independent audit firm. A third possibility would see the Government transfer the majority shares free of charge. This latest option would have the advantage of accelerating the ownership transfer process by eliminating or sharply abbreviating time-consuming steps such as valuation, marketing, and negotiations with buyers. However, it may not be politically palatable.

In addition, the transfer can take place either with immediate full payment or, as in the case of many other ownership transfers of publicly-owned organizations, with some form of deferred

[11] In the Bangladesh Grameen Bank, the borrowers now own about 92 percent of the shares in the Bank. In that case. the borrowers gradually bought the shares from over a ten year period, becoming majority shareholders after seven years. Today 9 of 12 Board members are elected by the borrowers.

payment scheme or leveraging. These aspects of any transfer will need to be worked out to see what is politically and financially feasible for both HMG/NRB and the ultimate buyers.

Option 1: Establishment of Foundation "Caretaker Owner" with Ultimate Transfer to Borrowers

In order to change the ownership in the near term, and eventually sell a majority of the shares to the women borrowers, the first option would be to establish a foundation. The foundation would be managed by a balanced combination of women borrowers, NGO leaders, and other individuals or organizations supporting the Grameen Bank development in Nepal. This foundation would be set up to purchase outright some percent of the shares in the GBBs from the government in the near term, so as to reduce the government's share from about 75 percent to below 50 percent, and possibly purchase enough for full or near-full divestiture.

The foundation would act as a holding company: initially holding in trust some 26 percent or more of the shares in each of the five government GBBs. With this level of ownership, the trustees of the foundation would be able to elect 2-3 Board members at each of the five GBBs. Those Board members would be able to exercise their corporate governance rights and responsibilities, thereby helping maintain professional management, and encouraging further development and expansion of the GBBs.

The foundation would have a limited life and would be legally set up to sell its shares progressively to women members of the GBBs, as soon as the GBB clients had sufficient funds to make these purchases. Depending on the valuation and sales price of the GBBs, and upon the savings mobilization of the GBBs, the life of the foundation is likely to cover some 3-10 years.

The private foundation is an option which the Government may wish to seriously consider. This foundation could help ensure the twin objectives of immediate ownership transfer and development of professional management structure for long-term sustainability. Involvement of donor agencies in the transfer/sale process as providers of technical assistance and operational support could enable the central bank to establish a private foundation which w-ould be managed independently and in the best interests of the borrower-members.

Option 2: Leveraged Buyout by Foundation

In this variation, the foundation w-ould be established, but would handle everything except for the financing of the initial share purchase. The government would transfer these shares to the foundation in return for some debt instrument (or other financial institutions might finance this. in return for deprived sector lending credits) incurred by each GBB on behalf of its borrowers, allowing for deferred payment once existing and new women clients buy the shares.

The foundation would provide management guidance and assist the women to develop their corporate governance skills, as well as helping maintain professional management, and encouraging further development and expansion of the GBBs. It would receive payments into an equity account as w-omen bought shares, paying these in turn to the debtors to retire the share-based debt.

As in Option 1, the foundation would have a limited life and would be legally set up to sell its shares progressively to w-omen members of the GBBs, as soon as the GBB clients had sufficient funds to make these purchases. Depending on the valuation and sales price of the GBBs, and upon the savings mobilization of the GBBs, the life of the foundation is likely to cover some 3 - 10 years.

Option 3: Immediate Sale/Transfer of Ownership to Borrowers

A favorable situation would call for the borrowers to become immediate majority shareholders by offering to buy 51 percent of the government share. Based on the Bangladesh Grameen experience, borrowers would be appropriate and responsible majority owners of the GBBs, since they have the biggest stake in the long-term success of the banks.

To be able to buy a majority share of the five banks some Rs. 115 million (US$ 2 million) will be required in capital, if GBB shares are sold at current book value, which the NRB has stated as its initial intention. To date, the borrowers have saved Rs. 41.2 million (US$ 723,000) in their group savings funds, and about half of that amount is needed by the borrowers themselves to meet temporary difficulties with payments and other consumption needs.

The current savings in the GBBs are not distributed evenly among individuals, borrowing groups, or by GBB. As a result, in addition to the overall limitation in the borrower savings. if share purchases are restricted to one share per borrower -- as is done in the Grameen Bank in Bangladesh -- an even smaller portion of the current total pool of savings would be available to borrowers to acquire shares. Many individual borrowers do not have the current level of savings in their accounts to buy even one share at the current book value price of Rs. 100 (US$ 1.75) per share. For this reason, at most only about half of the total savings would be available at this time to buy shares. As a result, the borrowers of GBBs are not at this time in a position to purchase enough shares outright to become majority shareholders.

It is conceivable that the purchase could be leveraged either with the NRB or with commercial banks, with women repaying the residual share cost over time as savings are accumulated and membership increases. However, a pay-later plan will probably not be sufficient to stave off undue non-professional, political interference.

The implementation of this option would result in a very slow process of up to ten years before the borrowers could become majority shareholders without debt, if transferred at book value.[12]

Option 4 -- Immediate Sale/Transfer of Ownership to NGOs

The third option could call for an NGO, or a consortium of NGOs, to buy a controlling or total share of the GBBs. This approach is appealing, in principle, since the mission and philosophy of the Grameen banks are consistent with the overall objectives and mission of the NGOs currently providing this kind of credit to the poor in Nepal.

There are, however, several reasons that might argue against this approach. The two NGOs in Nepal which provide Grameen-based micro-credit for the poor -- Nirdhan and CSD -- are still very small. Their short- and medium- term expansion and consolidation plans may not be compatible with such a major upscaling of their operations. In addition, the Government is not confident that these NGOs have the capacity to take over the GBBs and manage them efficiently.

If this option is to be given serious consideration, a more feasible alternative would have one or both of the NGO Grameens to purchase no more than one or two of the GBBs from the Government. This alternative would be more feasible from the NGOs' financial and management perspective, and has been explored inforrnally by one NGO Grameen during the last six months.

Option 5 -- Immediate Sale to Commercial Banks or Other For-Projit Companies

Under this option private banks or companies would be approached to purchase the controlling share in the Grameen Banks. On the positive side, the banks would bring good private sector management and corporate governance experience and skills to the GBBs. In addition, the higher GBB ownership stake by the commercial banks could contribute tow-ard meeting their deprived sector lending targets.

However, on the negative side, the limited profit potential of the GBBs strongly dampens most commercial bank and private company interest in taking a majority ownership in them. For this reason, the consultants believe the likelihood of finding interested buyers among the banking or business community in Nepal is quite low.

[12] It took about seven years for the borrowers of Bangladesh Grameen Bank to become majority shareholders. and the relative capitalization of the bank in Bangladesh was much lower.

Pros and Cons of Ownership Transfer Options		
Option	**Pros**	**Cons**
Option 1: Foundation Direct Buyout Model	Brings professional management to GBBs. Contributors to foundation provide capital to Government and allow for business-like terms of ownership transfer.	The foundation will not be the ultimate owner. Short-term focus on foundation establishment could be time-consuming. and act as distraction from main GBB mission. There may be reluctance to have any interim agency such as a foundation hold share ownership, even if only on a temporary basis.
Option 2: Foundation Management with Leveraged Buyout Model	Brings professional management to GBBs. Funds do not have to be raised from a donor to achieve the buyout, but can be arranged domestically. Members become immediate controllers of the GBBs.	Short-term focus on foundation establishment could be time-consuming: and act as distraction from main GBB mission. HMG and/or the commercial banks may be unwilling to finance the debt required to arrange the buyout.
Option 3: Borrower Model	Based on the Bangladesh Grameen experience, borrowers would be appropriate and responsible majority owners of the GBBs. Borrowers have the biggest stake in the long-term success of the Grameens.	The borrowers of GBBs are not in a position at this point to become majority or controlling shareholders. due to financial and management skills limitations. A pay later plan will probably not be sufficient to stave off political interference.

Option 4: NGO **Model**	Mission and philosophy of the NGOs are consistent with Grameen banks objectives and mission. Two NGOs are already providing this Grameen model credit delivery system to the poor in Nepal. A takeover of one or two GBBs with adjacent working areas may be possible and may make the newly merged organization more self-sufficient	The two NGO Grameens in Nepal already are fully extended with their short- and medium-term expansion and consolidation plans. The two NGO Grameens do not appear to have the financial and managerial capability to take over the ownership or management of the five GBBS at this time.
Option 5: Commercial Bank or Other For-Profit Owner Model	Commercial banks would bring good private sector management and corporate governance experience and skills to the GBBs. Higher GBB ownership stake could contribute tow-ard their deprived sector lending targets.	The limited profit potential of the GBBs strongly dampens most commercial bank and private company interest in taking a majority ownership in the GBBs at this stage in time.

Recommended Next Steps

The Nepal Rastra Bank and the Finance Ministry have indicated their interest and willingness to proceed with the ownership transfer. The next step would be to engage technical assistance which would facilitate ownership change through the following tasks and activities:

- present ownership change options to the Government of Nepal;
- assist with the selection of an ownership change option;
- undertake pre-sale valuation of the GBBs to be divested or partially divested, if needed;
- prepare a "prospectus" describing value, condition, legal status, and basic business plan of the GBBs offered for sale or partial sale, for use in discussing with w-omen clients and all other interested parties how the ownership transfer will work, as needed;
- ensure concurrence of existing owners and proposed buyers;
- prepare sales agreements; and
- assist with execution of the ownership change transactions.

USAID has asked the consultants to prepare terms of reference for this task. A Scope of Work for this technical assistance, including tasking, deliverables, staffing requirements, and a budget was prepared by the consultants, and is attached in Appendix B.

If USAID/NEPAL decides to proceed with the funding of the change of ownership assistance and implementation, it appears that this will be consistent with its women's empowerment Strategic Objective and USAID's overall Micro-enterprise Policy (9/95) by virtue of the following attributes:

- commitment to significant outreach of services;
- focus on women and the very poor;
- partnership with local organizations;
- adherence to rigorous performance standards;
- sharing best practices and fostering innovation and supportive policy change;
- micro-finance institutions should be committed to financial viability and have a credible plan for attaining it; and
- activities should be able to maintain levels of delinquency below- 10%, and loss rates below 5%; while charging interest rates and fees that enable the institution to achieve financial self -sufficiency.

In addition to meeting all of the above criteria, the policy direction of moving ownership from government to private hands (and particularly those of poor women borrowers) is consistent with other USAID strategies and objectives regarding economic growth and private sector development.

The consultants believe that the Government is aware of the importance and the sense of urgency in proceeding with the transfer/sale of its majority position in the GBBs. The Nepali Grameen replications together form the largest Grameen implementation worldwide, outside Bangladesh. The GBBs have proven to be an effective instrument for reaching poor w-omen.

The next most critical step is to move expeditiously and decisively to majority private ownership of the banks to ensure professional management and oversight, and to minimize the occurrence of political interference in the banks' operations. The proposed technical assistance program would provide assistance to the GBBs specifically to undertake that task. The objective would be to preserve all of the strengths of the present GBBs, while ensuring greater autonomy so as to minimize political pressures and influences on the banks, and ensure their continued rapid growth and achievement of full financial self-sustainability.

Appendix A - Tables

Table 1

OFFICE AND CREDIT OPERATIONS OF GBBs (As of mid-December 1996)					
Particular	**Eastern** GBB	**Western** GBB	**Mid-Western** GBB	**Far-Western** GBB	**Total**
A. Institutional Building					
t-lead Office	1	1	1	1	4
Area Office	7	1		3	11
Branch/Unit Office	39	9	8	21	77
Number of Centre	993	115	106	436	1,650
Total District Covered	5	4	3	4	16
Number of VDCs Covered	191	36	31	68	326
Total Staff	285	67	63	187	602
Number of Groups Formed	6,265	481	404	2,252	9,402
Number of Groups Members	31,267	2,405	2,016	11,420	47,108
B. Credit Operations (Amount In Rs. million)					
Amount Disbursed (Cumulative)	432.7	13.5	10.8	1 6	5 622
Numbe- of Borrowers	30,193	2,302	1,926	10,268	44,689
Amount Repaid (Cumulative)	311.8	6.8	5.3	120.1	444
Amount Overdue	0	0	C	0	0
Recovery Rate (%)	100	100	10C	100	100
Amount Outstanding	121	6.7	5.5	44.9	178
Savinas Mobilized (Rs. in Million)					
Group Fund	26.1	0.8	0.6	10.3	37.8
Personal Savinas	1.2	0.5	0.2	1.5	3.4

* This table does not include information on the fifth GBB, the Central Rural Development Bank.

Source: *GBBs*

Table 2

PROGRESS REPORT OF NIRDHAN & CSD As of Mid-December 1996			
Particular	**NIRDHAN**	**CSD**	**Total**
No. of District Covered	3	3	6
No. of Area Office	0	0	0
No. of Unit Office	7	11	18
VDC Covered	51	0	51
No. of Centers	223	216	439
No. of Groups	759	1,384	2,143
No of Group Members	3,795	6,452	10,247
No. of Borrowers	3,451	6,365	9,816
General Loan	**0**	**0**	**0**
Disbursed	34,808	32,744	67,552
Repayment	23,257	22,341	45,598
Outstanding	11,551	10,403	21,954
Special Loan	**0**	**0**	**0**
Disbursed	0	0	0
Repayment	0	0	0
Outstanding	0	0	0
Total	**0**	**0**	**0**
Disbursed	34,808	32,744	67,552
Repayment	23,257	22,341	45,598
Outstanding	11,551	10,403	21,954
Overdue	0	0	0
Group Fund	2,091	892	2,986
Group Fund Loan	**0**	**0**	**0**
Disbursed	0	0	0
Repayment	0	0	0
Outstanding	0	0	0
No. of Personal A/C	0	0	0
Personal Savings	447	1,544	1,991
Withdrawal from Personal a/c	0	1,017	1,017
Balance of Personal a/c	447	527	974
Total No. of Staff	97	0	97

Table 3

COMMERCIAL BANK'S LENDING TO GBBs
(As of mid-September 1996)

(Amount in Rs. million)

Commercial Banks	Eastern GBB		Far Western GBB	
	Amount	Interest Rate (%)	Amount	Interest Rate (%)
Nepal Bank Ltd.	20 ***20*** 10	6 ***8*** 6	40 ***20***	6 ***6.5***
Nepal Grindlays Bank	35	6	5	6
Nepal Indosuez Bank	5	6		
Nepal SBI Bank	3.2	6		
Nepal Bangladesh Bank	0.5	6		
Himalayan Bank				
Nepal Arab Bank				
Total	93.7		65	

Source: Nepal Rastra Bank

Table 4

SERVICE DELIVERY COST OF GBBs									
		Adminisi ive Cost (Rs. '000)			Loan Disbursement		Average Loan	Delivery Cost (Rs.)	
Institution/ Fiscal Year(**)	Number of Employee	Salary and Allowance	Other Admin. Cost*	Total	Number of Borrower	Amount (Rs. '000)	Disb. per Employee (Rs. '000)	Per Rupee Disbursed	Per Borrower
-1	-2	-3	-4	(5)=(3)+(4)	-6	-7	(8)=(7)/(2)	(9)=(5)/(7)	(10)=(5)/(6)
Far Western GBB									
1992/93#	50.0(	125.0(	521.00	646.01	18.01	60.00	1.20	10.77	35,889.00
1993194	118.0(	3,241.0(	2,174.00	5,415.0(	3,275.00	16,062.00	136.1 0	0.34	1,653.00
1994195	202.0(	7,487.0(	2,992.00	10.479.01	3,949.00	45,471.00	225.1 0	0.23	2,654.00
1995196	192.0(	9,944.0(	4,272.00	14,216.0(	1,992.00	73,054.00	380.50	0.19	7,338.00
Mid Western GBB									
1994/95@	20.0(	153.01	356.00	509.0(	75.01	356.00	17.80	1.43	6.787.00
1995/96	71.0(	1,545.0(	1,967.00	3,512.0(	1,228.00	5,901 .00	83.1 0	0.60	2,860.00
Western GBB									
1994/95++	16.0(	146.01	439.00	585.01	10.01	50.00	3.1 0	11.70	58.500.00
1995/96	58.0(	1,940.0(	2,503.00	4,443.0(	1,556.00	7,306.00	126.0 0	0 61	2,855.00
Eastern GBB									
1993194	149.0(	3,625.0(	2.452.00	6,077.0(	7,093.00	31,006.00	208.1 0	0.20	857.00
1994195	231.0(	9,517.0(	5,599.00	15,116.0(	14,445.00	117,789.00	509.9 0	0.13	1,046.00
1995/96	246.01	13,558.0(	5,746.00	19,304.0(	6,733.00	195,050.00	792.90	0.10	2.867.00
Nirdhan									
1992/93+++	8.0(	71.01	46.00	117.01	69.01	237.00	29.6 0	0.49	1,696.00
1993/94	16.0(	440.01	140.00	580.01	458.00	1,853.00	115.8 0	0.31	1,266.00
1994195	33.01	993.01	590.00	1,583.0(	1.486.00	9,065.00	274.70	0.17	1,065.00
1995/96	52.0(	1,674.0(	769.00	2,443.0(	2,811.00	15,119.00	290.80	0.16	896.00
SBP - CSD									
1993194	11 0(	149.01	86.00	235.0(	336.00	550.00	50.00	0.43	699.00
1994195	13.01	745.01	238.00	983.01	2,513.00	6,878.00	529.10	0.14	391 .00
1995/96	43.01	1,462.0(	459.00	1,921.0(	5,096.00	16,901 .00	393.00	0.11	377.00

Source: Eastern, Western, Mid-Western and Far-Western Rural Development Banks, Nirdhan and CSD

* Does not include interest paid on the borrowings

\# Lost 15 days of the fiscal year

@ Last 58 days of the fiscal year

++ Last one day of the fiscal year

+++ Last four months of the fiscal year

(**) Fiscal year ends on mid-July

Table 5

SHAREHOLDERS OF GBBs AND THEIR PAID-UP CAPITAL*

(Rs. millions)

Name of Shareholders	Eastern		Central		Western		Mid-Western		Far-Western	
	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total
1. HMG	4.95	8.25%			9.9	16.50%	9.9	16.50%	4.95	8.25%
2. Nepal Rastra Bank	40.05	66.75%	44.4	74.00%	36.6	61.00%	37.9	63.17%	40.05	66.75%
3. Nepal Bank Lt.	3	5.00%	3	5.00%	3	5.00%	3	5.00%	3	5.00%
4. Rastriya Banijya Bank	3	5.00%	3	5.00%	3	5.00%	3	5.00%	3	5.00%
5. Nepal Arab Bank Ltd.	3	5.00%					3	5.00%	1.5	2.50%
6. Nepal Indosuez Bank Ltd.	3	5.00%			1.5	2.50%			3	5.00%
7. Nepal Grindlays Bank	3	5.00%							3	5.00%
8. Himalayan Bank Ltd.					3	5.00%				
9. Nepal SBI Bank Ltd.							3	5.00%		
10. Nepal Bargladesh Bank			3	5.00%	3	5.00%				
11. Agricultural Dev. Bank			3	5.00%						
12. Bank of Kathmandu			3	5.00%						
13. Credit Guarantee Corp.			0.5	1.00%			0.2	0.33%		
Total	60	100.00%	63	100.00%	60	100.00%	60	100.00%	58.5	97.50%

***Authorized capital Rs. 120 million each, and Issued capital Rs. 60 million each for 4 banks, except Rs. 70 million for Central Dev. Region.**

Source: Nepal Rastra Bank

Table 6

EASTERN GRAMEEN DEVELOPMENT BANK LTD.
at end of Mid-July 1996
Balance Sheet

Last Year	Liabilities	Rs.	Current Year	Last Year	Assets	Rs.	Current Year
120000000	Authorized capital		Rs	Rs.			
	1200000 @Rs 100		120.000.000	14,420,165	Cash & Bank A/C		15,935,766
					(Annex - 3)		
60000000	Issued & pad up capital			560,764	Cash	1,768,412	
	600000 @ Rs 100		60,000,000	13,859,401	Bank	14,167,354	
580000	Reserved Fund		783,432	71,458,917	Loan Investment		119,180,513
	General Reserve			70,122,300	Loan to members	117,057,253	
580000	Capital Reserve	744,432		540,237	Saving Loan	1,673,627	
	Staff Welfare fund	39,000		796,380	Irrigation Loan	449,633	
36119744	Loan (Annex -1)		85,527,870	4,632,497	Fixed Asset (Annex 4)		4,857,919
	External Loan	2272,000					
36119744	Internal Loan	83,255,870			Other Asset (Annex - 5)		17,889,129
					Inventory	2,403,606	
10758590	Saving & Deposit		23.322.892		Sundry Debtors	12,702,534	
9061580	Group Saving	21,157,851			Staff Advance	2,782,989	
84145	Emergency Saving	395,491					
1612865	Personal Saving	1,770,050			Profit & Loss A/C		28,621,680
					Previous Year	17,659,016	
					Current Year	10,962,664	
9787663	Other Provision & Liabilities (Annex 2)		15,874,391				
65297	Staff Provident Fund		39,949				
610413	Internal Branch A/C		936,473	117,921,707			
117921707	Total		186,485,007		Total		186,485,007

Table 7

EASTERN GRAMEEN BIKAS BANK LTD. for the year ended Mid-July 1996. Profit & Loss A/C							
Last Year	Expenses	Rs.	Current Year	Last Year	Income	Rs.	Current Year
1.434.882	Interest Expenses		4,056,769	3.534.891	nterest Income		11,945,816
404,032	Saving/Deposit	1,050,576		2,998,956	.oan Investment	11,338,7	
1,030,851	Loan	3.456.19:3		535,863	)ther Investment	607,04	
9,516,865	Personal Expenses		13,557,809	39,791	)ther income		998,175
8,172,620	Salary	10,923,10 0			)epreciation on Assets (Grant Received)		115,610
388,746	Staff Provident Fund	624,251			Net Loss C/D		
955,499	Other	2,010,458		2,976,000	Balance Sheet)		10,962,664
5,412,926	Office Operating Cost		5,745,636				
10,630	Loss from Exchange (Currency Exchange)		44,673				
	Employee Welfare fund		50,000				
175,306	Provision for Risk		116,716				
			24,022,265				24,022,265

Table 8

FAR WESTERN GRAMEEN BIKAS BANK

Central Office

Dhangadhi

BALANCE SHEET as at 2053 Ashadh last (Mid of July 1996), Rs.

Previous Year	Liabilities		Amount	Previous Year	Assets		Amount
	Share capital			1,341,369.82	Cash in hand		2,290,842.79
120,000,000	Authorized share capital		120,000,000		(Including Cash in Transit)		
	(12,00,000 ordinary shares of			3,198,649.34	Bank Balance		5,531,100.39
	Rs. 1 00/- per share)			198,050.62	Nepal Rastra Bark	3,381,252.47	
57,000,000	Issued & Paid-up Capital		58,500,000	1,263,649.79	Nepal Bank Ltd.	1,055,118.79	
	(585,000 Ordinary shares of			465472.26	Rastriya Banijya Bank	1,076,023.49	
	Rs. 100/- per share)			1,261,476.67	Himalayan Bank Ltd.	14,699.85	
	Advance against Shares			10,000.00	Indosuez Bank Ltd.	4,005.79	
75,053	Reserve Fund		75,053	76,000,000.00	Investments		60,400,000.00
57,418,894	Loans from commercial balks		60,175,070	18,500,000.00	Govt. Securities	60,400,000.00	
				57,500,000.00	Fixed Deposits		
5,128,435	Deposits		10,474,907	27,196,140.00	Loans & Credits		46,200,444.00
3,790,871	Group Fund	8434612.71		23,512,949.00	General Loan	37,412,719.00	
1,294,448	Personal Saving	1890408.3:		562,316.00	Group Fund Loar	1,346,507.00	
43,116	Others	149886.'		3,120,875.00	Miscellaneous Loan	7,441,218.00	
3,707,834	Other provision &liabilities		12,713,571	4,170,417.49	Fixed assets		4,851,941.12
255,973	Inter-office accounts		67,337	2,179,745.43	Other assets		6,039,407.64
	Profit & Loss account			190,743.74	Closing stock	177,337.16	
	Previous year			1,598,022.04	Sundry debtors	3,034,480.53	
	Current year			390,979.65	Staff acvances	2,827,589.95	
				9,499,867.44	Profit & Loss account		16,692,262.59
				2,948,712.64	Previous year	9,499,867.44	
				6,551,154.80	Current year	7,197,395.15	
123,586,190			142,005,999	1 23,586,189.52			142,005,998.53

Table 9

FAR WESTERN GRAMEEN BANK LTD.
Profit & Loss A/C
for the year ended Mid-July 1996

Rs.

Last Year	Income		Amount
5,856,416	Interest Income		11,180,265
2,204,634	Interest on Loans	4,787,515	
3,648,539	Investment	6,364,556	
3,244	Other interest Income	28,193	
124,182	Other Income		49,923
	Grant		121,205
	income From Sale of Assets		225
6,551 ,1 55	Net Loss c/d in Balance Sheet		7,192,395
12,531,754			**18,544,013**

Last Year	Expenses		Amount
2,007,403	Interest Expenses		4,282,40
229,795	Deposit	**523,331**	
59,893	Other Interest Expenses	**160,657**	
	(Interest on Employee Provident Fund		
1,71 7,715	Interest in Loan	3,598,420	
7,487,422	Personal Expenses		9,944,03(
5,730,296	Salary	8,210,611	
312,213	Provident Fund	521,243	
1,444,913	Other Personal Expenses.	1,212,176	
	Office Operating Cost		
2,991,681	Provision for Risk	4,272,026	4,272,02(
45,248	Write off of bad loan.	45,550	45,551
12,531,754	**Net profit**		**18,544,01:**

Appendix B - Terms of Reference

OWNERSHIP TRANSFER OF GRAMEEN BIKAS BANKS IN NEPAL

Background

Expanding the access of the poor to financial services is one of Nepal's mechanisms for alleviating poverty. In 1992, His Majesty's Government (HMG) decided to establish five Grameen Bank replications, one for each of the five development regions in Nepal. The first to commence were the Eastern and Far Western Grameen Bikas Banks (GBBs); the last one is now being finalized in the Central Region. Two NGO Grameen replications. Nirdhan and the Center for Self-Help Development (CSD), are also operating in Nepal.

The GBBs were capitalized with 60 million Nepali Rupees each, with 60 percent coming from the Nepal Rastra Bank (NRB, or central bank), 15 percent from HMG, and the remainder from private sector banks. (This investment is counted as an allocation against their priority sector lending requirement.) The Board Chairman for three GBBs is one of the two Deputy Governors of the NRB, and the other Deputy Governor chairs the other two. The Managing Directors have been frequently changed, with new appointees following each change of government; the Eastern GBB, the oldest one, has had three Managing Directors in the last three years.

In their operations, the Eastern GBB has received a small amount of financial support from the Grameen Trust in Bangladesh, and has received a working capital injection of Rs. 100 million from the NRB. The other GBBs have operated from their share capital and borrowings from domestic commercial banks to date.

A recent USAID funded consultancy', undertaken through the IRIS project, emphasized the importance of quickly moving to majority private ownership. According to that report, such a move would have a very favorable impact on the future expansion and viability prospects of the GBBs.

Although the NRB has established the mechanism for transfer of ownership on the basis that it would have group savings buy into the shares, in practice this is proving a very slow mechanism for ownership transfer. The NRB has also recognized that as the central bank, it has a pivotal role to foster micro-finance growth, but not necessarily through direct operations.

See the "The Impact of Ownership on the Grameen Bikas Bank's Current and Future Performance" by Dr. Muzammel Huq and Mr. Peter Boone.

Objective

The objective of this consultancy is to assist the Government of Nepal to identify and carry out viable, locally acceptable methods for the transfer of ownership of the Grameen Bikas Banks from the NRB and HMG.

Scope of Activity

There are seven tasks to be performed by a team anticipated to include:

- one privatization specialist,
- one Grameen Bank/micro-credit professional,
- one financial analyst/valuation specialist, and
- one legal advisor.

The total professional level of effort is estimated to be 24 person months over a 12 month period.

Tasks to be Performed:

1. **Present ownership change options to the Government of Nepal.** Under this task the consultants will suggest options for change in ownership structure. carefully considering the economic and financial environment, the likelihood that the banks will not reach financial self-sufficiency for some time, and the political and legal requirements.

   Options for potential consideration include, but are not limited, to the following:

   - merger and collective divestiture;
   - divestiture into a foundation with private sector trustees;
   - sale/transfer to borrowers;
   - selective or collective buyout by an NGO; or
   - selective or collective takeover as subsidiaries of private sector banks;

2. **Assist the NRB and HMG in the selection of an ownership change option.** A clear ownership change option and plan should be finalized by month 3 of the consultancy.

3. **Undertake pre-sale valuation of the GBBs to be divested or partially divested,** This task should be undertaken by an individual or an accounting firm with extensive experience in auditing, valuation, and pricing issues prior to ownership change.

4. **Prepare a "prospectus" describing value, condition, legal status, and basic business plan of the GBBs offered for sale or partial sale.** The "prospectus" should be useful as part of the due diligence process and also in the marketing of the banks to prospective buyers.

5. **Ensure concurrence of existing owners and proposed buyers.** As part of the discussion process, the consultants should build consensus with all the important stakeholders in the process such as existing owners, borrowers, and proposed buyers.

6. **Prepare sales agreements.** The consultants will prepare contractual sales agreements which will be negotiated and approved by existing owners and new buyers.

7. **Assist with execution of the ownership change transactions.** The final task is the most important one -- assisting with the execution of the ownership change transaction. This step will determine the success of the consultancy, and ultimately the future prospects of the GBBs.

Each of these tasks will require discussions with the staff and management of each of the five GBBs, and with selected clients in the field; review of their finances and other records; discussions with selected GBB members; review of NRB records and other information on their performance; and detailed talks and consensus building with key decision-makers regarding the political and economic acceptability of the proposed alternatives.

Duration and Level of Effort

This consultancy is anticipated to require 24 person-months of technical assistance. The duration of the technical assistance is 12 calendar months.

Roles and Responsibilities

The Nepal Rastra Bank will oversee the work, with the Governor or his designate handling oversight. Logistics inside Nepal will be jointly arranged by the NRB and the consultant. The Nepal Rastra Bank will second a senior officer with key knowledge of the GBBs and personnel for the period of the consultancy. HMG should request the technical assistance and confirm its commitment to the ownership change prior to commencing the technical assistance.

Deliverables Expected

1. Preparation of a detailed Work Plan.
2. Weekly meetings with the NRB to discuss progress and issues.
3. Monthly meetings with USAID/Nepal to discuss progress and issues.
4. Presentation of ownership change options and select ownership change option with the Government of Nepal.
5. Pre-sale valuation of the GBBs to be divested or partially divested.
6. A “prospectus” describing value, condition, legal status, and basic business plan of the GBBs offered for sale or partial sale.
7. Transfer agreements.
8. A final report mentioning issues and lessons learned in the process.

Consultant Qualifications

The privatization specialist should have solid experience working on ownership and divestiture issues. Experience in the financial sector, and with unorthodox organizations which are not expected to be profitable, is desirable. International experience, including handling financial sector ownership issues in Third World countries is required. Past experience in Nepal is desirable.

The Grameen Bank/micro-credit professional should have a long history of experience in both micro-credit and Grameen Bank operations, with special skills in Grameen Bank financing. S/he should have a minimum of 10 years of progressively responsible experience in this field. Experience in the Third World is required and past experience in Nepal is desirable.

The financial analyst/valuation specialist should have extensive experience in the valuation and pricing of companies using alternative valuation methods. She/he should have a minimum of 5 years experience in financial analysis/valuation and pricing, preferably in a Third World setting, and including privatization/valuation work in the financial sector.

The legal advisor should have extensive experience in legal transfer of ownership issues including the preparation of prospectuses and the drafting of sales agreements. She/he should have a minimum of 10 years experience in law, including experience in privatization law, mergers and acquisitions, banking laws, company law, and NGO/foundation law.

Fluency in English is required for all the consultants.

Budget and Payment Terms

The total estimated cost of the consultancy is US$ 1,5 10,000. These costs include; professional services costs of US$ 960,000; administrative and logistical costs of US$ 300,000: travel and per diem cost of US$ 200,000 and miscellaneous/contingency costs of US$ 50,000.

Appendix C - List of People Interviewed

Nepal Rastra Bank

Mr. Satyendra P. Shrestha
Governor

Mr. Bharat K. Sharma
Deputy Governor

Mr. Prafula K. Kafle
Deputy Governor

Mr. Ram Babu Pant
Chief Manager

Mr Shalik Ram Sharma
Chief Manager

Mr. Bhagat Bista
Deputy Chief Manager

Mr. Ganesh Kumar Threstha
Deputy Chief Manager

Ministrv of Finance

Mr. Mahat
Minister of Finance

Mr. Ram Binod Bhattarai
Secretary

Mr. Keshab B. Kharty
Under Secretary

Grameen Bikas Banks

Mr. Prakash Raj Sharma
Acting Director
Far Western Grameen Bikas Bank

Mr. Rewat Karki
Executive Director
Mid Western Grarneen Bikas Bank

Executive Directors
Western Grameen Bikas Bank, Eastern Grameen Bikas Bank

NGO Grameens

Dr. H.D. Pant
Executive Director
Nirdhan

Mr. Shankar Man Shrestha
Executive Director
CSD

Commercial Banks

Mr. Prithivi B. Pande
Executive Director
Himalayan Bank Limited

USAID

Ms. Jane Nandy
Team Leader/S03

Ms. Shubha Banskota
Program Officer, SO3/IR3

Asian Develonment Bank

Mr. Marshuk Ali Shah
Resident Representative
Nepal Resident Mission

Mr. Raghu Adhikary
Project Implementation Officer
Nepal Resident Mission